

BOARD MEETING DATE: June 6, 2008

AGENDA NO. XX

PROPOSAL: Adopt Rule 314 – Fees for Architectural Coatings

SYNOPSIS: Proposed Rule 314 - Fees for Architectural Coatings sets fees for manufacturers of architectural coatings to recover the cost of AQMD programs, and will provide staff with architectural coating quantity and emissions information for planning, compliance, and rule development.

COMMITTEE: Stationary Source, February 15, 2008, April 25, 2008 and May 16, 2008; Administrative April 11, 2008 Reviewed

**RECOMMENDED ACTION:**

Adopt the attached resolution:

1. Certifying the Notice of Exemption for Proposed Rule 314 – Fees for Architectural Coatings; and
2. Adopt Rule 314 – Fees for Architectural Coatings.

Barry R. Wallerstein, D.Env.  
Executive Officer

EC:LT:LB

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**Background**

The AQMD's fee system has evolved over the years. In 1990, KPMG Peat Marwick performed a Fee Assessment Study which determined, among other things, that permit processing fees did not fully cover the costs of performing this program and recommended a flat emissions fee for low emitters, which was ultimately, adopted a number of years later. In 1995, KPMG Peat Marwick completed a second Fee Assessment Study which again recommended increasing permit processing fees, but also recommended an "emissions based operating fee" which would be based on potential to emit rather than actual emissions. Industry generally opposed this concept

and it was not adopted. In 1999, the AQMD retained Thompson, Cobb, Bazilio & Associates, P.C., Certified Public Accountants and Management Consultants, to conduct an independent analysis of the stationary source fee structure. The AQMD also established a Fee Structure Advisory Committee, composed of representatives from industry, including small businesses, environmental groups, and AQMD staff. The report recognized that area source non-permitted VOC emissions, such as architectural coatings, were the bulk of stationary emissions and should be the target for AQMD control and revenue generation efforts. However, the potential number of sources was beyond the number manageable through a traditional permitting program. The most significant problem that control of area sources posed was enforcement of regulations. Obtaining the cooperation of a large population of consumers and collecting information on sources and emissions would be an overwhelming task. A successful program would have to be focused on a smaller population, such as manufacturers or distributors of the regulated products. At the same time the program would have to collect fees to fund program operations.

During Fiscal Year 2000-2001 the Governing Board directed staff to establish a special Revenue Committee to assist the AQMD in developing revisions to its fee rules to stabilize revenue. The major focus of this committee's effort was the identification and assessment of several short- and long-term potential funding sources in support of AQMD programs as well as the costs. The Revenue Committee made several important recommendations that were included in the rule amendments approved by the Governing Board in May 2001. One of the recommendations was a fee on area sources. The Committee also recommended a manufacturers' fee for area sources. In June 2004, the Governing Board, in response to this recommendation, adopted fees to recover the costs associated with notification and tracking of emissions from decontamination of soil projects; recovery of costs associated with laboratory analysis of non-compliant samples taken in the field for compliance verification; recovery of Plan audits, verification, evaluation, inspection and tracking costs for area source rules such as open burning and old vehicle scrapping; and fees for enforcement inspections for statewide registered portable equipment, which are all considered area sources.

At the Board's direction to assess fees on area sources, staff is proposing Rule 314 to recover the cost of regulating the architectural coatings program, one of the largest controlled emitters of VOC emissions in the AQMD, and include that program's fair share of AQMD costs that are apportioned among all AQMD programs, such as air monitoring, the Multiple Air Toxics Study, etc. The proposed rule will also provide staff with architectural coating quantity and emissions information for planning, compliance, and rule development. The cost of the Proposed Rule 1113 Program, which includes the strengthening of the enforcement and laboratory efforts dedicated to the program, is projected to be approximately \$4.2 million, which equates to approximately 7.1¢ per

gallon, based on estimated quantity of coatings, and is anticipated to be passed on to the end-user by the manufacturers. Staff estimates the proposed rule will impact approximately 200 architectural coatings manufacturers.

With an estimated 15,000 sources including registered contractors and architectural coating retail stores (does not include architects, specifiers, non-registered contractors, active painting sites and the do-it-yourself market) regulated by Rule 1113, the proposed program should result in approximately 3,000 inspections per year with 750 to 800 samples of architectural coatings collected for laboratory VOC analysis to determine compliance, which is considered to be statistically significant to assess a supportable compliance rate.

### **Proposal**

Proposed Rule 314 requires Architectural Coatings Manufacturers, which distribute or sell their manufactured architectural coatings into or within the AQMD for use in the AQMD and are subject to Rule 1113 - Architectural Coatings, to submit an Annual Quantity and Emissions Report beginning in 2009 and each subsequent calendar year for the previous calendar year. The proposed fees, when fully implemented, will be 3.6 cents per gallon and \$246 per ton of VOC emissions. Fees will be phased-in over three years with the fee rate set in 2009 to recover approximately one-half the cost of the Rule 1113 Program, three-fourths of the cost in 2010 and the full cost of the Program recovered in subsequent years. The fee will be determined based on the quantity of coatings as well as the cumulative emissions from the quantity of coatings distributed or sold for use in the AQMD.

The proposed rule noticed for public hearing on June 6, 2008, has been amended to include a requirement for architectural coatings manufacturers to provide a list to the AQMD of all their distributors located in the U.S.; an exemption for fees for any coatings containing 5 or less grams of VOC per liter of material to further incentivize the development, marketing and use of lower-VOC coatings; and other language clarifying the intent of the proposal.

### **Key Issues**

During the rulemaking process, staff has resolved numerous issues presented by industry, including withdrawing the pre-registration requirements and special labeling requirements, developing a simplified fee structure, and proposing a phased-in fee over three years. However, staff was unable to resolve some of industry's concerns, which are summarized below:

Issue: More time is need for rulemaking.

Response: Staff extended the rulemaking scheduling by postponing the public hearing from February to June 2008 in order to meet with NPCA and

other industry members to resolve concerns pertaining to rule language, fee structure, and the reporting form and have made significant progress. Although some issues remain, a further delay in the rulemaking may not result in further significant progress in resolving those issues. Further delay would also compress the initial implementation schedule. Sufficient time for companies to adjust to this fee program has been one of the concerns expressed by the industry that we have attempted to address as the proposed rule has evolved. An example is the proposed three year phase-in.

Issue: An enhanced compliance program is unnecessary.

Response: Currently, there is only one inspector FTE allocated to Rule 1113 – Architectural Coatings enforcement, even though this area source continues to be one of the largest emitters of VOCs (23 tons per day in 2010) within our regulatory authority and non-compliance could result in significant excess emissions. The current level of enforcement results in so few inspections and coating samples for analysis that they are considered to be statistically insignificant to ascertain a compliance rate. As with any other program, enforcement of the rule is the key to safeguarding emission reductions. Staff has discussed the need for the proposed enhanced compliance program with the industry, and has a detailed assessment justifying the need for more compliance presence in the staff report. Further, in the adopting resolution, staff has committed to a review and report on the implementation of the program enhancement.

Issue: CARB Fees are duplicative for the same emissions

Response: Although CARB is involved with certain aspects of Architectural Coatings program, their activities are not the same as those the AQMD is mandated to do for air quality, including the implementation of an adequate regulatory program for architectural coatings. Staff believes the most equitable way to assess fees to recover our costs for the architectural coatings program is to apply them to the coating manufacturers based on quantity sold and emissions. CARB has also elected to assess fees to recover their costs to coating manufacturers based on emissions.

Issue: The proposed rule does not provide incentive to lower emissions.

Response: The emission fee component is designed to provide an incentive to lower emissions. Further, the revised staff proposal includes an

exemption for fees for any coatings with 5 or less grams of VOC per liter of material to further incentivize the development, marketing and use of lower-VOC coatings.

**Issue:** Manufacturers have expressed concerns about paying fees that will be used to support enforcement efforts directed at end users.

**Response:** Staff has revised the proposal so that one FTE to be devoted to end-user enforcement will be supported by other AQMD revenues, and has reduced the anticipated revenues and fee rate for the quantity-based fee accordingly.

**Issue:** Subsequent to the set hearing for Proposed Rule 314, the National Paint and Coatings Association (NPCA) wrote to the AQMD that the proposed rule is unfair because it only applies to manufacturers who distribute or sell their manufactured architectural coatings into or within the AQMD, excluding those distributors that ship coatings into the AQMD from warehouses located outside the AQMD, which NPCA stated may account for 10% to 15% of the volume sold in the AQMD. However, in a follow-up letter, NPCA estimated that amount may be larger since architectural coatings sold through mass merchant or “big box” stores are 30% of total sales on a national basis.

**Response** During the rule development process, staff’s initial proposal required manufacturers to account for all the volume of coatings they manufacture, supply, sell, offer for sale or solicit for sale for use in the AQMD. Some manufacturers said that it would be too burdensome to track their manufactured coatings once they were released to a second or third party distributor and they were not sure the distributors would provide them with an accurate volume count. NPCA said the unaccounted architectural coatings volume was believed to be small (NPCA did not provide the requested volume) and probably a wash considering that some coatings were shipped into the AQMD and then later shipped out of the AQMD without being subtracted from the total volume. NPCA said this is the same agreement manufacturers have with CARB to report architectural coatings for CARB Surveys and related fees. However, in response to NPCAs most recent comments, dated April 21, 2008, which are contradictory to their earlier written and oral comments requesting to exclude the volume of coatings distributed outside the AQMD, staff has amended the proposed rule to require manufacturers to provide the AQMD with a list of all their U.S. distributors on an annual basis. Staff is then committed to working with distributors to try and determine the extent of architectural coatings that

may not be accounted for in the proposed required annual quantity and emissions reports. Staff can then make a determination in the future as to whether the unreported volume justifies requiring distributors to be considered for inclusion in the proposed rule. Staff has contacted several major manufacturers that sell architectural coatings to “big box” stores and those manufacturers have stated that they track sales into the AQMD particularly for compliance purposes, considering that AQMD Rule 1113 – Architectural Coatings has more stringent VOC limits than other parts of California and the U.S. Since these manufacturers are able to track detailed volume distributed to these “big box” stores, staff believes the majority of the coatings distributed to these stores will be reported.

### **Emission Inventory and Emission Reduction**

The proposed rule does not explicitly affect air quality or emissions although the proposed fee structure may provide an incentive to a manufacturer to lower total emissions by marketing a larger volume of low VOC coatings. Staff does not plan to claim any emission reductions in the State Implementation Plan (SIP) as a result of this fee program.

### **CEQA**

The AQMD has reviewed the proposed project pursuant to State CEQA Guidelines §15002(k)(1). Proposed fee Rule 314 is exempt pursuant to CEQA Guidelines §15273. A Notice of Exemption has been prepared in accordance with state CEQA Guidelines §15062 for the proposed project and will be filed with the county clerks immediately following the adoption of the proposed rule. A copy has been included as an attachment to this Board letter.

### **Socioeconomic Analysis**

The proposed amendments do not directly affect air quality or emissions limitations. Therefore, a socioeconomic assessment is not necessary or required. Nonetheless, staff conducted a socioeconomic analysis to assess the total impacts for all the actors in the four-county economy and it was determined that the cost of this rule would have few impacts on the relative cost of production and delivered price for all the industries in the four-county area. As a result, the proposed rule is not expected to have impacts on competitiveness at the industry level.

### **Authority to Assess Fees**

California Health and Safety Code Section 40522.5 establishes the AQMD’s authority to adopt a schedule of fees to be assessed on areawide or indirect sources of emissions which are regulated, but for which permits are not issued, to recover the costs of programs related to these sources. Under California law, the primary authority for controlling emissions from architectural coatings is vested in the air pollution control

districts (APCDs).

### **Implementations and Resources**

The Architectural Coatings Program began in 1977. For the past 10 to 15 years the AQMD has allocated approximately 8 full time equivalent positions to the Architectural Coatings Program at a current cost of \$2.44 million which includes the architectural coatings program's fair share of emissions fee supported program costs such as air monitoring. Staff is proposing to enhance the current Program to a total of 18 full time equivalent positions that upon final implementation over three years will be funded in total by architectural coatings manufacturers at a cost of approximately \$4.2 million. One inspector FTE will be funded through other resources and will focus on end-user inspections, including thinning practices and it is anticipated that the share of end-user related laboratory fees that are not paid by the end-users themselves will be supported by other AQMD resources and included in the "one inspector FTE." The enhanced program is necessary to ensure the SIP committed VOC emission reductions for architectural coatings are real, permanent, quantifiable, and enforceable.

### **Attachments**

- A. Summary of Proposed Amendments
- B. Rule Development Process Flow Chart
- C. Key Contacts
- D. Resolution
- E. Rule Language
- F. Final Staff Report
- G. Final Staff Report, Appendix A, Table 1
- H. CEQA – Notice of Exemption

## ATTACHMENT A

### Summary of Proposed Amendments to Rule 314 – Fees for Architectural Coatings

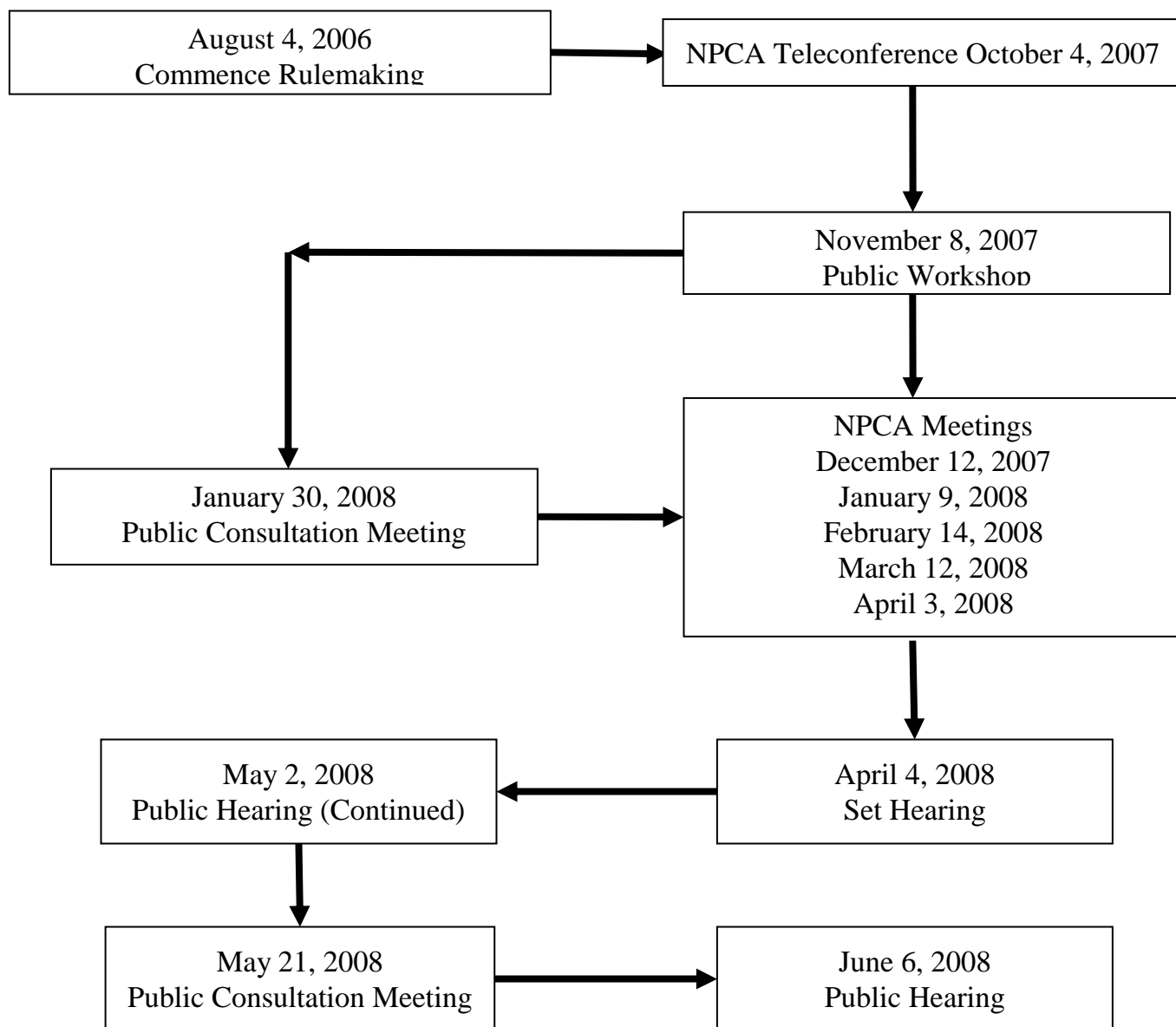
- Architectural Coatings Manufacturers that distribute or sell products into and within the District must:
  - Apply for a manufacturer identification (ID) number.
  - Submit an Annual Quantity and Emissions Report certified by a Responsible Party.
  - Maintain sufficient records to verify data necessary to determine annual architectural coating sales and VOC emissions in the AQMD, and compliance with applicable rules and regulations.
- Proposed Fee Structure:
  - \$168.62 for a Manufacturer ID number application, and
  - The annual quantity of architectural coatings distributed or sold into or within the AQMD for use in the AQMD and their associated VOC emissions. The proposed fees at full implementation are 3.6 cents per gallon and \$246 per ton of VOC emissions. Fees will be phased-in over three years, beginning 2009 for sales and associated emissions reported in 2008 and fully implemented in 2011 and each subsequent calendar year for the sales and associated emissions for the previous calendar year.
  - Coatings with 5 grams or less of VOC per liter of material are exempt from the quantity and emissions fees.
- Procedures for:
  - Amending the Annual Quantity and Emissions Reports,
  - Refund of fees for overpayment, and
  - Fee payments and late filing surcharges.
- A provision for the confidentiality of reported information subject to the provisions of the California Public Records Act.
- A violation section that states “It shall be a violation of this rule for any Architectural Coatings Manufacturer that does not have a manufacturer ID number issued by the AQMD to distribute or sell their manufactured architectural coatings into or within the AQMD for use in the AQMD.”
- Test methods as specified in Rule 1113 to determine VOC content of the coatings.
- Amendments are proposed to the rule originally noticed for public hearing on May 2, 2008 that include a requirement for architectural coatings manufacturers to provide a list to the AQMD of all their distributors located in the U.S. in order for staff to investigate the amount of coatings entering the AQMD from distributors outside the AQMD.



## ATTACHMENT B

### RULE DEVELOPMENT PROCESS

#### PROPOSED AMENDED RULE 314 – Fees for Architectural Coatings



Total Time Spent in Rule Development: 22 Months

## ATTACHMENT C

<b><u>KEY CONTACTS</u></b>		
<b>Mike</b>	<b>Butler</b>	<b>Behr</b>
<b>Jennifer</b>	<b>Wolfenden</b>	<b>Benjamin Moore</b>
<b>Billy</b>	<b>Evans</b>	<b>Dunn-Edwards Paint</b>
<b>Robert</b>	<b>Wendoll</b>	<b>Dunn-Edwards Paints</b>
<b>Howard</b>	<b>Berman</b>	<b>Dutko Worldwide</b>
<b>Marl</b>	<b>Barbour</b>	<b>Eastman</b>
<b>Patrick</b>	<b>Lutz</b>	<b>EPs/CCA</b>
<b>Joseph</b>	<b>Tashjian</b>	<b>Ellis Paint Company</b>
<b>Fred</b>	<b>Anwari</b>	<b>Frazee Paint</b>
<b>Fernando</b>	<b>Pedroza</b>	<b>Frazee Paint</b>
<b>Jeff</b>	<b>Margulies</b>	<b>Fulbright &amp; Jaworski</b>
<b>Jim</b>	<b>Kantola</b>	<b>ICI Paints</b>
<b>Jim</b>	<b>Boyce</b>	<b>Insl-X Superior Coating System</b>
<b>John</b>	<b>Day</b>	<b>Henry Company</b>
<b>Curtis</b>	<b>Coleman</b>	<b>Law Offices of Curtis Coleman</b>
<b>Robert</b>	<b>Gross</b>	<b>PPG Architectural Finishes, Inc.</b>
<b>Dwayne</b>	<b>Fuhlhage</b>	<b>PROSOCO</b>
<b>Dave</b>	<b>Darling</b>	<b>National Paint &amp; Coatings Association</b>
<b>Alison</b>	<b>Keane</b>	<b>National Paint &amp; Coatings Association</b>
<b>James</b>	<b>Baker</b>	<b>RCMA</b>
<b>Madelyn</b>	<b>Harding</b>	<b>Sherwin-Williams Company</b>
<b>Richard</b>	<b>Mikol</b>	<b>Tremco</b>
<b>Paul</b>	<b>Sara</b>	<b>Valspar</b>
<b>Mike</b>	<b>Kacner</b>	<b>Valspar</b>
<b>John</b>	<b>Long</b>	<b>Vista Paint Corporation</b>
<b>Dave</b>	<b>Carey</b>	<b>W.R. Meadows</b>
<b>Catherine</b>	<b>Jacobson</b>	<b>3M</b>